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BEFORE THE ARIZONA CORPORATION COMMISSION

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IN THE MATTER OF THE APPLICATION OF
ARIZONA WATER COMPANY, AN ARIZONA
CORPORATION, FOR ADJUSTMENTS TO ITS
RATES AND CHARGES FOR UTILITY SERVICE
FURNISHED BY ITS WESTERN GROUP AND FOR
CERTAIN RELATED APPROVALS.

DOCKET NO. W-01445A-04-0650

Staff's Notice of Filing

The Utilities Division ("Staff") hereby provides notice of filing of Supplemental Testimony
of Staff Witness Steven M. Olea.

RESPECTFULLY SUBMITTED this 16 day of June 2005.


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of the foregoing were filed this
16 day of June 2005 with:

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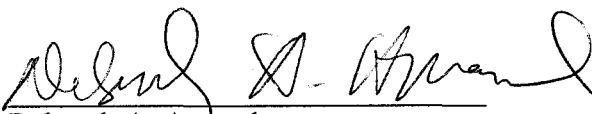
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BEFORE THE ARIZONA CORPORATION COMMISSION

JEFF HATCH-MILLER

Chairman

WILLIAM A. MUNDELL

Commissioner

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MIKE GLEASON

Commissioner

KRISTIN K. MAYES

Commissioner

IN THE MATTER OF THE APPLICATION OF)
ARIZONA WATER COMPANY, INC. FOR A)
DETERMINATION OF THE CURRENT FAIR)
VALUE OF ITS UTILITY PLANT AND)
PROPERTY AND FOR INCREASES IN ITS)
RATE CHARGES FOR UTILITY SERVICE)
BASED THEREON)
_____)

DOCKET NO. W-01445A-04-0650

SUPPLEMENTAL

TESTIMONY

OF

STEVEN M. OLEA

ASSISTANT DIRECTOR

UTILITIES DIVISION

ARIZONA CORPORATION COMMISSION

JUNE 16, 2005

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I. INTRODUCTION

Q. Please state your name and business address.

A. Steven M. Olea, 1200 West Washington, Phoenix, Arizona, 85007.

Q. By whom and in what capacity are you employed?

A. I am employed by the Arizona Corporation Commission ("Commission") as the Assistant Director for the Utilities Division ("Division").

Q. Please state your educational background.

A. I graduated from Arizona State University ("ASU") in 1976 with a Bachelors Degree in Civil Engineering. From 1976 to 1978, I obtained 47 graduate hours of credit in Environmental Engineering at ASU.

Q. Please state your pertinent work experience.

A. From April 1978 to October 1978, I worked for the Engineering Services Section of the Bureau of Air Quality Control in the Arizona Department of Health Services ("ADHS"). My responsibilities were to inspect air pollution sources to determine compliance with ADHS rules and regulations.

From November 1978 to July 1982, I was with the Technical Review Unit of the Bureau of Water Quality Control ("BWQC") in ADHS (this is now part of the Arizona Department of Environmental Quality ["ADEQ"]). My responsibilities were to review water and wastewater construction plans for compliance with ADHS rules, regulations, and Engineering Bulletins.

1 From July 1982 to August 1983, I was with the Central Regional Office, BWQC, ADHS.
2 My responsibilities were to conduct construction inspections of water and wastewater
3 facilities to determine compliance with plans approved by the Technical Review Unit. I also
4 performed routine operation and maintenance inspections to determine compliance with
5 ADHS rules and regulations, and compliance with United States Environmental Protection
6 Agency requirements.

7
8 From August 1983 to August 1986, I was a Utilities Consultant/Water-Wastewater Engineer
9 with the Division. My responsibilities were to provide engineering analyses of Commission
10 regulated water and wastewater utilities for rate cases, financing cases, and consumer
11 complaint cases. I also provided testimony at hearings for those cases.

12
13 From August 1986 to August 1990, I was the Engineering Supervisor for the Division. My
14 primary responsibility was to oversee the activities of the Engineering Section, which
15 included one technician and eight Utilities Consultants. The Utilities Consultants included
16 one Telecommunications Engineer, three Electrical Engineers, and four Water-Wastewater
17 Engineers. I also assisted the Chief Engineer and performed some of the same tasks as I did
18 as a Utilities Consultant.

19
20 In August 1990, I was promoted to the position of Chief Engineer. My duties were
21 somewhat the same as when I was the Engineering Supervisor, except that now I was less
22 involved with the day-to-day supervision of the Engineering Staff and more involved with
23 the administrative and policy aspects of the Engineering Section.
24

1 In April 2000, I was promoted to my present position as one of two Assistant Directors of the
2 Division. In this position, I assist the Division Director in the policy aspects of the Division.
3 I am primarily responsible for matters dealing with water and energy.
4

5 **II. PURPOSE**

6 **Q. What was your assignment in this case?**

7 A. Since the retirement of Mr. Lyndon R. Hammon, I am assigned to sponsor his direct
8 testimony in the case of Arizona Water Company's ("Company") application for a rate
9 increase. Mr. Hammon was the Division Staff ("Staff") engineering witness. In addition, I
10 will be sponsoring the major portion of Staff's testimony with regard the Central Arizona
11 Project ("CAP") deferred Municipal and Industrial ("M&I") capital charges dealing mostly
12 with the policy aspects. Mr. Darron Carlson will be discussing the accounting issues
13 regarding these charges.
14

15 **III. CAP HOOK-UP FEE**

16 **Q. In its surrebuttal testimony, Staff stated that it would explain its position with regard to**
17 **Company's CAP rebuttal testimony by the time of the hearing due to settlement**
18 **discussions on this issue with the Company. Was a settlement agreement achieved?**

19 A. No.
20

21 **Q. Based on the Company's rebuttal testimony, has Staff revised its position with regard**
22 **to the treatment of deferred and on-going CAP M&I capital charges?**

23 A. Staff has not changed its overall position, but does have some revisions to some of the details
24 of its position.

1 **Q. Please explain.**

2 A. Staff's overall position was that the Company should not be allowed to include its deferred
3 and/or on-going CAP M&I capital charges in rate base and, therefore, not be able to recover
4 these costs until it could somehow demonstrate that it would actually be using a substantial
5 portion of its CAP allocations to serve customers. It is Staff's opinion that this position was
6 and is in general agreement with the "**Proposed** Policy for Central Arizona Project ("CAP")
7 Cost Recovery" ("Proposed Policy") (emphasis added) posted on the Commission's website.
8 Thus, Staff's overall position remains the same.

9
10 With regard to the details, Staff now recommends that without including the CAP M&I
11 capital charges in rate base, the Company be allowed to begin recovering these charges
12 through a CAP Hook-up Fee Tariff with conditions. The CAP Hook-up Fees that Staff is
13 recommending are attached as Schedules SMO-1, SMO-2 and SMO-3. The conditions for
14 approval of these tariffs are attached as Schedules SMO-4. The charges described in these
15 tariffs are based on a 20-year amortization.

16
17 **Q. Where you involved in developing the Proposed Policy?**

18 A. Yes.

19
20 **Q. Was the Proposed Policy ever approved by the Commission?**

21 A. As nothing more than a proposed policy.
22

1 **Q. Before you explain why Staff is modifying its position with regard to the details of CAP**
2 **cost recovery, please explain why you highlighted the word “Proposed” in your**
3 **preceding answer.**

4 A. In reading the Company’s rebuttal testimony it seems to Staff that the Company believes that
5 the Proposed Policy is either a hard and fast policy of the Commission to which the Staff
6 must adhere or even a rule that would require Commission permission in order to deviate
7 from it. If this is the indeed the Company’s position, Staff would strongly disagree. The
8 Proposed Policy is neither a hard and fast policy nor a rule, but at best a reference. It should
9 be noted that the Proposed Policy was originated in 2000 yet to this day, the Commission has
10 not taken any formal action on it; therefore, it remains a proposed policy. That is exactly
11 why Staff referred to the Proposed Policy in its Direct Testimony (and this testimony’s)
12 recommendations. Staff believes these recommendations are appropriate for this company in
13 this case.

14
15 **Q. Now would you please explain why Staff is modifying its position with regard to the**
16 **details of CAP cost recovery?**

17 A. In its Direct Testimony, Staff stated that the Company could begin recovery of prudently
18 incurred CAP costs after its next rate case if it filed a detailed CAP water use plan by
19 December 31, 2006, demonstrating that the Company would be using a significant portion of
20 its CAP allocations to serve its customers by 2010. This testimony was based on Staff’s
21 opinion that the Company’s Direct Testimony did not contain enough information to allow
22 CAP cost recovery in this present rate case.

23
24 Staff believes that the Company’s rebuttal testimony provides additional information that
25 demonstrates a more concrete commitment to actually use its CAP allocations. Based on this
26 information, Staff believes that it is in the public interest to allow the Company to begin

1 recovery of its prudently incurred CAP M&I capital charges (both deferred and on-going) in
2 this rate case through the attached tariffs, but only with the conditions attached as Schedule
3 SMO-4.
4

5 **Q. Does this conclude your testimony?**

6 **A.** Yes, it does.
7

TARIFF SCHEDULE

UTILITY: Arizona Water Company
DOCKET NO.: W-01445A-04-0650

DECISION NO. _____
EFFECTIVE DATE: _____

**CENTRAL ARIZONA PROJECT HOOK-UP FEE
for
CASA GRANDE SYSTEM**

I. Purpose and Applicability

The purpose of the Central Arizona Project ("CAP") Water Hook-up Fee ("CAP Fee") payable to **Arizona Water Company** ("the Company") pursuant to this tariff is to equitably apportion the costs of CAP water. These charges are applicable to all new service connections established after the effective date of the tariff. The charges are one-time charges and are payable as a condition to the Company's establishment of service, as more particularly provided below.

II. Definitions

Unless the context otherwise requires, the definitions set forth in R-14-2-401 of the Arizona Corporation Commission's ("Commission") rules and regulations governing water utilities shall apply in interpreting, this tariff schedule.

"Applicant" means any party entering into an agreement with the Company for the installation of water facilities to serve new service connections.

"CAP costs" means Commission allowed on-going and deferred costs known as Municipal and Industrial capital charges incurred by the Company with regard to its CAP water allocations. These costs shall include allowance for funds used during construction which rate shall be the Company's annual cost of debt.

"Company" means Arizona Water Company, an Arizona corporation.

"Main Extension Agreement" means any agreement whereby an applicant agrees to advance the costs of the installation of water facilities to the Company to serve new service connections, or install water facilities to serve new service connections and transfer ownership of such water facilities to the Company, which agreement shall require the approval of the Commission's Utilities Division (same as line extension agreement).

"Service Connection" means and includes all service connections for residential, commercial, industrial, or other uses, regardless of meter size except for temporary services and separate fire protection services.

III. CAP Hook-up Fee Charges

Each new service connection shall pay the CAP Fee derived from the following table:

Meter Size	Fee
5/8" x 3/4"	\$220
3/4"	\$220
1"	\$220
1-1/2"	\$733
2"	\$1,173
3"	\$2,347
4"	\$3,667
6" or larger	\$7,333

IV. Terms and Conditions

- (A) Assessment of One Time CAP Fee: The CAP Fee may be assessed only once per service connection, or lot within a platted subdivision (similar to service line and meter installation charges). However, this provision does not exempt from the CAP Fee, any newly created parcel(s) which are the result of further subdivision of a lot or land parcel and which do not have a service connection.
- (B) Use of CAP Fee: CAP Fees may only be used to pay for CAP costs as defined herein. CAP Fees shall not be used for expenses, maintenance, or operational purposes.
- (C) Time of Payment:
- (1) In the event that the Applicant is required to enter into a main extension agreement, whereby the Applicant agrees to advance the costs of installing mains, valves, fittings, hydrants and other on-site improvements in order to extend service in accordance with R-14-2-406(B), payment of the charges required hereunder shall be made by the Applicant within 15 calendar days after receipt of notification from the Company that the Utilities Division of the Commission has approved the main extension agreement in accordance with R-14-2-406(M).
 - (2) In the event the Applicant is not required to enter into a main extension agreement, the charges hereunder shall be due and payable at the time the service is initially established.
- (D) Failure to Pay Charges, Delinquent Payments: Under no circumstances will the Company set a meter or otherwise allow service to be established if the Applicant has not paid in full all charges as provided by this CAP Fee tariff.

- (E) CAP Fee Non-refundable: The amounts collected by the Company pursuant to this CAP Fee Tariff shall be non-refundable.
- (F) Use of Charges Received: All funds collected by the Company as CAP Fees shall be used solely for the purpose of paying for CAP costs as defined herein.
- (G) CAP Fee in Addition to Other Charges: The CAP Fee shall be in addition to any costs associated with a main extension agreement for on-site facilities, and are in addition to the amounts to be advanced pursuant to charges authorized under other sections of this tariff.
- (H) Termination of CAP Fee: The CAP fee shall be terminated when all CAP costs (as defined herein) have been collected or when ordered by the Commission, whichever occurs first.

TARIFF SCHEDULE

UTILITY: Arizona Water Company
DOCKET NO.: W-01445A-04-0650

DECISION NO. _____
EFFECTIVE DATE: _____

CENTRAL ARIZONA PROJECT HOOK-UP FEE for COOLIDGE SYSTEM

I. Purpose and Applicability

The purpose of the Central Arizona Project ("CAP") Water Hook-up Fee ("CAP Fee") payable to **Arizona Water Company** ("the Company") pursuant to this tariff is to equitably apportion the costs of CAP water. These charges are applicable to all new service connections established after the effective date of the tariff. The charges are one-time charges and are payable as a condition to the Company's establishment of service, as more particularly provided below.

II. Definitions

Unless the context otherwise requires, the definitions set forth in R-14-2-401 of the Arizona Corporation Commission's ("Commission") rules and regulations governing water utilities shall apply in interpreting, this tariff schedule.

"Applicant" means any party entering into an agreement with the Company for the installation of water facilities to serve new service connections.

"CAP costs" means Commission allowed on-going and deferred costs known as Municipal and Industrial capital charges incurred by the Company with regard to its CAP water allocations. These costs shall include allowance for funds used during construction which rate shall be the Company's annual cost of debt.

"Company" means Arizona Water Company, an Arizona corporation.

"Main Extension Agreement" means any agreement whereby an applicant agrees to advance the costs of the installation of water facilities to the Company to serve new service connections, or install water facilities to serve new service connections and transfer ownership of such water facilities to the Company, which agreement shall require the approval of the Commission's Utilities Division (same as line extension agreement).

"Service Connection" means and includes all service connections for residential, commercial, industrial, or other uses, regardless of meter size except for temporary services and separate fire protection services.

III. CAP Hook-up Fee Charges

Each new service connection shall pay the CAP Fee derived from the following table:

Meter Size	Fee
5/8" x 3/4"	\$150
3/4"	\$150
1"	\$150
1-1/2"	\$500
2"	\$800
3"	\$1,600
4"	\$2,500
6" or larger	\$5,000

IV. Terms and Conditions

- (A) Assessment of One Time CAP Fee: The CAP Fee may be assessed only once per service connection, or lot within a platted subdivision (similar to service line and meter installation charges). However, this provision does not exempt from the CAP Fee, any newly created parcel(s) which are the result of further subdivision of a lot or land parcel and which do not have a service connection.
- (B) Use of CAP Fee: CAP Fees may only be used to pay for CAP costs as defined herein. CAP Fees shall not be used for expenses, maintenance, or operational purposes.
- (C) Time of Payment:
- (1) In the event that the Applicant is required to enter into a main extension agreement, whereby the Applicant agrees to advance the costs of installing mains, valves, fittings, hydrants and other on-site improvements in order to extend service in accordance with R-14-2-406(B), payment of the charges required hereunder shall be made by the Applicant within 15 calendar days after receipt of notification from the Company that the Utilities Division of the Commission has approved the main extension agreement in accordance with R-14-2-406(M).
 - (2) In the event the Applicant is not required to enter into a main extension agreement, the charges hereunder shall be due and payable at the time the service is initially established.
- (D) Failure to Pay Charges, Delinquent Payments: Under no circumstances will the Company set a meter or otherwise allow service to be established if the Applicant has not paid in full all charges as provided by this CAP Fee tariff.

- (E) CAP Fee Non-refundable: The amounts collected by the Company pursuant to this CAP Fee Tariff shall be non-refundable.
- (F) Use of Charges Received: All funds collected by the Company as CAP Fees shall be used solely for the purpose of paying for CAP costs as defined herein.
- (G) CAP Fee in Addition to Other Charges: The CAP Fee shall be in addition to any costs associated with a main extension agreement for on-site facilities, and are in addition to the amounts to be advanced pursuant to charges authorized under other sections of this tariff.
- (H) Termination of CAP Fee: The CAP fee shall be terminated when all CAP costs (as defined herein) have been collected or when ordered by the Commission, whichever occurs first.

TARIFF SCHEDULE

UTILITY: Arizona Water Company
DOCKET NO.: W-01445A-04-0650

DECISION NO. _____
EFFECTIVE DATE: _____

**CENTRAL ARIZONA PROJECT HOOK-UP FEE
for
WHITE TANKS SYSTEM**

I. Purpose and Applicability

The purpose of the Central Arizona Project ("CAP") Water Hook-up Fee ("CAP Fee") payable to **Arizona Water Company** ("the Company") pursuant to this tariff is to equitably apportion the costs of CAP water. These charges are applicable to all new service connections established after the effective date of the tariff. The charges are one-time charges and are payable as a condition to the Company's establishment of service, as more particularly provided below.

II. Definitions

Unless the context otherwise requires, the definitions set forth in R-14-2-401 of the Arizona Corporation Commission's ("Commission") rules and regulations governing water utilities shall apply in interpreting, this tariff schedule.

"Applicant" means any party entering into an agreement with the Company for the installation of water facilities to serve new service connections.

"CAP costs" means Commission allowed on-going and deferred costs known as Municipal and Industrial capital charges incurred by the Company with regard to its CAP water allocations. These costs shall include allowance for funds used during construction which rate shall be the Company's annual cost of debt.

"Company" means Arizona Water Company, an Arizona corporation.

"Main Extension Agreement" means any agreement whereby an applicant agrees to advance the costs of the installation of water facilities to the Company to serve new service connections, or install water facilities to serve new service connections and transfer ownership of such water facilities to the Company, which agreement shall require the approval of the Commission's Utilities Division (same as line extension agreement).

"Service Connection" means and includes all service connections for residential, commercial, industrial, or other uses, regardless of meter size except for temporary services and separate fire protection services.

III. CAP Hook-up Fee Charges

Each new service connection shall pay the CAP Fee derived from the following table:

Meter Size	Fee
5/8" x 3/4"	\$500
3/4"	\$500
1"	\$500
1-1/2"	\$1,667
2"	\$2,667
3"	\$5,333
4"	\$8,333
6" or larger	\$16,667

IV. Terms and Conditions

- (A) Assessment of One Time CAP Fee: The CAP Fee may be assessed only once per service connection, or lot within a platted subdivision (similar to service line and meter installation charges). However, this provision does not exempt from the CAP Fee, any newly created parcel(s) which are the result of further subdivision of a lot or land parcel and which do not have a service connection.
- (B) Use of CAP Fee: CAP Fees may only be used to pay for CAP costs as defined herein. CAP Fees shall not be used for expenses, maintenance, or operational purposes.
- (C) Time of Payment:
- (1) In the event that the Applicant is required to enter into a main extension agreement, whereby the Applicant agrees to advance the costs of installing mains, valves, fittings, hydrants and other on-site improvements in order to extend service in accordance with R-14-2-406(B), payment of the charges required hereunder shall be made by the Applicant within 15 calendar days after receipt of notification from the Company that the Utilities Division of the Commission has approved the main extension agreement in accordance with R-14-2-406(M).
 - (2) In the event the Applicant is not required to enter into a main extension agreement, the charges hereunder shall be due and payable at the time the service is initially established.
- (D) Failure to Pay Charges, Delinquent Payments: Under no circumstances will the Company set a meter or otherwise allow service to be established if the Applicant has not paid in full all charges as provided by this CAP Fee tariff.

- (E) CAP Fee Non-refundable: The amounts collected by the Company pursuant to this CAP Fee Tariff shall be non-refundable.
- (F) Use of Charges Received: All funds collected by the Company as CAP Fees shall be used solely for the purpose of paying for CAP costs as defined herein.
- (G) CAP Fee in Addition to Other Charges: The CAP Fee shall be in addition to any costs associated with a main extension agreement for on-site facilities, and are in addition to the amounts to be advanced pursuant to charges authorized under other sections of this tariff.
- (H) Termination of CAP Fee: The CAP fee shall be terminated when all CAP costs (as defined herein) have been collected or when ordered by the Commission, whichever occurs first.

CONDITIONS FOR APPROVAL OF CAP HOOK-UP FEE

1. Arizona Water Company ("AWC") must submit by December 31, 2006, or six months prior to submission if its next rate case application, whichever comes first, a detailed Central Arizona Project Water Use Plan ("CAPWUP") for its Western Group water systems.
2. AWC must make best faith efforts to include the cities of Casa Grande and Coolidge in the development of the CAPWUP.
3. The CAPWUP must address all the issues outlined in Attachment A.
4. The CAPWUP must be approved by Staff prior to AWC's next rate case application being declared sufficient under A.A.C. R14-2-103.
5. The CAPWUP shall be approved, disapproved, or modified in AWC's next rate case by the Commission. If the CAPWUP is disapproved, the CAP Hook-up Fee shall be terminated and AWC shall refund all CAP Hook-up Fee monies collected to that point along with six percent (6%) interest. The refund method shall be determined by the Commission.
6. The approval by Staff or the Commission of the CAPWUP shall mean only that the CAPWUP has adequately addressed all the issues outlined in Attachment A. CAPWUP approval by Staff or the Commission shall **not** be interpreted as a used and useful determination nor as pre-approval of reimbursement of any future expenditures in completing the plan.
7. In AWC's next rate case the Commission shall reevaluate this CAP Hook-up Fee to determine if it should be continued, eliminated or modified based on the CAPWUP and any other evidence that may be introduced by parties to that case.
8. If in AWC's next rate case the Commission orders continuation of the CAP hook-up fee or any other recovery mechanism designed to recover CAP deferrals, the Commission Staff shall audit the CAP deferral accounts of AWC's systems holding CAP allocations and shall make any necessary adjustments, true-ups, and re-calculations to determine the proper values to carry forward.
9. Staff will utilize AWC's annual cost of debt to determine the rate for allowance of funds used during construction ("AFUDC") included in the CAP deferrals.

CENTRAL ARIZONA PROJECT WATER USE PLAN (“CAPWUP”)

The plan should address the following:

1. Existing water supplies and demand patterns for the last two years (such information as required on the Water Use Data Sheet).
2. Future water supplies and demand patterns demonstrating how and when CAP water will be used through the year 2025. All future water sources other than CAP should be discussed. All assumptions used to make projections should be clearly explained.
3. All major infrastructure components required to use CAP water through the year 2025 should be listed and described in as much detail as possible. These would include such items as, but not be limited to, treatment plants, transmission mains, storage tanks, pumping stations, etc.
4. Projected capital and Operation and Maintenance costs for all future water supplies (including CAP water) through the year 2025 should be listed in as much detail as possible. All assumptions used to make these projections should be clearly explained.
5. How CAP water will be used to address the arsenic issue (if it will be).